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C O N F I D E N T I A L SECTION 01 OF 02 TAIPEI 000244

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TAGS: ECON EINV ETTC PGOV PREL TW CH
SUBJECT: SEMICONDUCTOR ENTREPRENEUR EXPLAINS TAIWAN STRENGTHS

REF: 06 TAIPEI 4164

Classified By: AIT Director Stephen M. Young, Reason 1.4 d

¶1. (C) Summary: Powerchip Semiconductor Chairman Frank Huang told the AIT Director on January 30 that Taiwan semiconductor firms will keep their global competitive advantage of cost-effective production. He commented that Chinese competitors in the industry will not be the threat to Taiwan firms that many had expected. Huang opposes restrictions on semiconductor investment in the PRC because he believes Taiwan firms will limit investment in order to protect corporate secrets. He foresees improved economic prospects after 2008 with improved cross-Strait relations regardless of who wins the presidential election that year. End summary.

¶2. (C) AIT Director Young met with Powerchip Semiconductor Corporation Chairman Frank Huang on January 30 to discuss Taiwan's economic prospects and the future of the global semiconductor industry. Powerchip is Taiwan's largest maker of dynamic random access memory (DRAM) chips and Taiwan's third largest semiconductor manufacturer overall. It operates three 12-inch wafer manufacturing facilities in Taiwan and recently entered into a US$14 billion joint venture with Japan's Elpida Memory Inc. to build four more. Its revenue rose 79 percent in 2006 to US$2.8 billion, while profits were up 325 percent.

Taiwan's Hi-Tech Competitive Edge Will Continue

¶3. (C) Huang believes Taiwan will stay competitive and maintain its prominent place in the global semiconductor industry. He explained to the Director that in logic chips, Intel is still on top globally and no one at this point is in a position to challenge it. However, in DRAM chips, Taiwan, Japanese, South Korean and U.S. firms are all producing technologically similar products. According to Huang, in earlier stages of the DRAM industry, technology was more important, but now cost-effective production is the key to profitability. This, he said, is an area where Taiwan excels. Huang commented that Japanese firms in the industry are less competitive because they don't fear elimination like their smaller and newer Taiwan competitors and in turn their employees

are less motivated. He further explained that in DRAM, brand names don't matter because memory prices vary only slightly between companies. Using his other firm, Umax Technologies, as an example, Huang described how he had been able to build a fairly successful brand name in scanners. However, eventually he was unable to compete with larger companies like HP, which have more capital and brand recognition.

China's Semiconductor Challenge Has Faded

¶4. (C) Turning to China's role in the semiconductor industry, Huang expressed confidence that Taiwan firms would maintain their advantages over Chinese competitors both in technology and profitability. He noted that five years ago many industry observers talked about the rapid advance of China's Semiconductor Manufacturing International Corporation (SMIC) and the possibility that it might eventually eclipse Taiwan Semiconductor Manufacturing Company (TSMC), the world's largest contract chip manufacturer. However, as Huang pointed out, these predictions have not materialized; TSMC has maintained and strengthened its domination of the contract chip making market, while SMIC has not been as profitable as many expected. Huang commented that Richard Chang, the Taiwan-born Chairman of SMIC, "is no Morris Chang," TSMC's Chairman. If SMIC couldn't catch up with Taiwan in the past few years, it will take many more years, he said.

Lift the Restrictions - Taiwan Firms Will Stay
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¶5. (C) Huang argued that restrictions on semiconductor investment were unnecessary and instead Taiwan should let semiconductor manufacturers decide how much to risk on investment in the PRC. He emphasized the difficulty semiconductor firms have retaining employees in the Mainland. Because employees frequently leave to work for competitors, it is almost impossible to protect corporate secrets there, he said. Because of this danger, Huang

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believes Taiwan semiconductor firms will not invest more than 20 percent of their capacity in China. He implied that Powerchip would not move quickly to begin construction of a semiconductor plant in the PRC since receiving approval from the Ministry of Economic Affairs in December 2006 (reftel). He backed away from media reports that Powerchip would build its China plant in Suzhou, noting that he was looking at inland locations as well. Away from China's more prosperous coastal provinces, employee turnover might not be as high.

Powerchip Open to Takeover Possibility

¶6. (C) When the Director asked if Taiwan stocks were undervalued, Huang agreed strongly. He believes that improved relations with China would help increase values by attracting more U.S. investment. Huang commented that Powerchip was open to the possibility of being acquired by a foreign investor in a deal similar to Carlyle Group's recent proposal to buy Advanced Semiconductor Engineering. However, he reported that Powerchip was not currently in discussions with any potential buyers.

Economy Will Improve After 2008 Election

¶7. (C) Huang expects economic conditions in Taiwan to improve after the 2008 election as a result of improved relations with the PRC. He believes that the Democratic Progressive Party (DPP) will be more flexible on cross-

Strait relations after President Chen Shui-bian leaves office. Huang praised the DPP for taking action when necessary, singling out Premier Su Tseng-chang for moving quickly when a problem appears. He called the DPP "street smart" with the ability to get things done. In contrast, he characterized the Pan-Blue parties as well-educated elites. According to Huang, their tendency is listen to a problem, talk, and then make proposals. However, he stated that his firm did not look for active government support. Instead, Powerchip lobbies for policies that will allow the firm to compete in the global market.

Comment

¶8. (C) Dynamic innovators like Frank Huang make it easy to look toward Taiwan's economic future with optimism. An American-educated MD, he shifted from medical research to Taiwan-based hi-tech entrepreneurship in the roaring eighties, and has built a multi-billion dollar operation in the past twenty years. Neither he nor Powerchip show any signs of slowing down any time soon. When the Director asked Huang how long his joint venture with Elpida would last, he lowered his voice conspiratorially and whispered "Forever!"
YOUNG